VZCZCXYZ0003
PP RUEHWEB

DE RUEHLP #1191/01 1241949
ZNR UUUUU ZZH
P 041949Z MAY 06
FM AMEMBASSY LA PAZ
TO RUEHC/SECSTATE WASHDC PRIORITY 9067
INFO RUEHAC/AMEMBASSY ASUNCION 5809
RUEHBO/AMEMBASSY BOGOTA 3106
RUEHBR/AMEMBASSY BRASILIA 6968
RUEHBU/AMEMBASSY BUENOS AIRES 4214
RUEHCV/AMEMBASSY CARACAS 1507
RUEHPE/AMEMBASSY LIMA 1484
RUEHMD/AMEMBASSY MADRID 3097
RUEHMN/AMEMBASSY MONTEVIDEO 3753
RUEHFR/AMEMBASSY PARIS 0077
RUEHQT/AMEMBASSY QUITO 4147
RUEHSG/AMEMBASSY SANTIAGO 8693
RUEHBS/USEU BRUSSELS
RHEHNSC/NSC WASHINGTON DC
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RUCPDOC/DEPT OF COMMERCE WASHINGTON DC
RUEATRS/DEPT OF TREASURY WASHINGTON DC

UNCLAS LA PAZ 001191

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STATE FOR WHA/AND
TREASURY FOR SGOOCH
ENERGY FOR CDAY AND SLADISLAW

E.O. 12958: N/A
TAGS: ECON EINV ENRG EPET BL
SUBJECT: NATIONALIZATION: COMPANY PERSPECTIVES

REF: A. LA PAZ 1157

¶B. LA PAZ 1159

¶1. (SBU) Summary: While foreign investors were not surprised by most of the terms of the GOB's May 1 nationalization decree (ref A), they were nonetheless taken aback that their long-dreaded expectations appeared to have become reality. So far most companies have reacted in measured fashion, and reportedly plan to continue negotiating with the government. The Hydrocarbons Chamber President speculated that no company would proceed to arbitration in the short term. U.S.-invested companies, particularly Chaco and Transredes, are worried about the GOB's plan to gain ownership control over their operations. Brazil has publicly expressed its concern about ensuring domestic gas supply and protecting investor rights, which are threatened by the GOB's plan to nationalize Brazilian-owned refineries, increase taxes attributable to Petrobras, and raise gas prices. Brazilian-owned Petrobras, which previously took a conciliatory tone with the GOB, ratcheted up its response on May 3, threatening to halt all investment and to initiate arbitration. The Brazilian, Argentine and Venezuelan presidents are meeting with President Morales today (May 4) to discuss the decree. Spain has also publicly expressed its discontent over the decree and reportedly plans to send a delegation to Bolivia. End summary.

Waiting for the Smoke to Clear

¶2. (SBU) Foreign investors had no reason to be surprised by most of the terms of the GOB's May 1 decree "nationalizing" the country's hydrocarbons resources, but that didn't stop them from feeling shock that long-dreaded expectations appeared to have become a reality. So far, most companies have taken a measured public response, as though waiting for the smoke to clear. An advisor to Repsol told us that, apart from the temporary 32% tax increase on operators in

mega-fields, it remained unclear what the decree had concretely changed. He said the decree had been mostly political, and intended to shore up the government's base as the Constituent Assembly campaign got underway (ref B). At the same time, the decree had also conveyed the government's hard-line starting position on negotiating new contracts, for which it allowed six months, and that the results of those negotiations were what mattered most.

Hydrocarbons Chamber: Companies will Negotiate
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¶3. (SBU) Bolivian Hydrocarbons Chamber President, Enrique Menacho, told us the Chamber issued a cautious press statement in response to the decree expressing concern that the GOB had unilaterally and negatively altered the conditions under which companies must operate and counterproductively impacted legal security and investment promotion, but that the Chamber would try to promote a productive dialogue between the companies and the GOB. Menacho told us that his impression from a May 2 meeting the Chamber had held with company representatives was that the companies would continue to seek negotiations with the government and refrain from initiating arbitration -- which he described as a last resort -- at least in the short term. He added that the GOB and Venezuelan auditors (ref A) were investigating the companies in order to pressure and weaken them in the run up to negotiations with the government. He stated that the GOB's 32 percent increased taxation of fields producing more than 100 million cubic feet per day could cause a production decrease.

U.S. Company Perspectives: Chaco, Transredes, GTB, Vintage
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¶4. (SBU) U.S. companies have invested roughly USD 800

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million in Bolivia's hydrocarbons sector. Of these, the two companies that invested in enterprises that had been owned by the state before being "capitalized" -- Pan-American and Prisma -- would likely be most impacted by the decree. Chaco (Pan-American) executive, Jana Drakic, told us on May 2 that the company was particularly concerned about the GOB's plan to acquire 50 percent plus one of its shares. She said the GOB had not discussed acquiring the shares with Chaco, and that it was unclear whether the GOB intended to purchase or expropriate them. She explained that the pension funds held approximately 49 percent of the company's shares, and that after confiscating those from the Bolivian public, the GOB would need to obtain an additional 1 percent plus one share from U.S. and Argentine private investors to gain majority control. Drakic added that roughly 80 percent of pension payments directed to elderly Bolivian retirees currently came from Chaco, Repsol Andina, and Transredes, the three capitalized hydrocarbons companies, and said she did not know how the GOB would continue to make these payments after these pension fund shares had been confiscated and transferred to YPFB (the state oil company). Drakic said that news reports of military occupation were exaggerated, and that less than 20 (compared with 56 reported in the news) installations had a military presence.

¶5. (SBU) Transredes (Prisma, pipeline operator) executive, Maria Claudia Dabdoub, told us the company would continue negotiating with the GOB, but (echoing her Chaco counterpart) did not know how the GOB would seek to acquire majority ownership of the company. Dabdoub explained that only 34 percent of Transredes was held by Bolivian pension funds, while 16 percent was held by private individuals, 25 percent by Shell, and 25 percent by Prisma. Thus, after the GOB confiscated the pension fund shares, it would still need to obtain 16 percent plus one. Dabdoub doubted that Prisma or Shell would be willing to sell these shares. She added that YPFB staff had told her that Transredes' foreign executives would be replaced by Bolivians after the take-over. She noted that the military occupation had created an unpleasant working environment, in which all staff were searched entering and exiting the offices to ensure that they were not removing documents.

¶6. (SBU) GTB (U.S.-invested pipeline operator that is 51 percent owned by Transredes) President Ed Miller said that the GOB had neither met with them nor provided them with a model contract. He said that the GOB's potential plan to expropriate shares, name board presidents, and take control of corporations was contrary to Bolivian law. He expressed his concern that the Transredes Board could be infiltrated by YPFB members, which might then attempt to take over seats on the GTB board, on which 2 of 5 positions are held by Transredes. He was also concerned about the GOB audits being conducted in part by Venezuelans. He claimed that such audits would be used to "find irregularities, which could be found at any company, and blow them out of proportion" in order to gain negotiating leverage. He heard that up to 50 Venezuelan auditors had been contracted by the GOB at a rate of USD 2 million to inspect the hydrocarbons companies. Dabdoub confirmed that Venezuelan auditors had been in Bolivia for more than one week.

¶7. (SBU) Vintage Petroleum (Occidental), a relatively small producer, told us that the decree would have a minimal impact on its operations, in comparison with the already enacted May 2005 Hydrocarbons Law. As a producer with small fields, the law provides for a lower than average tax rate, even though the relevant regulations have not yet been promulgated. Moreover, he said, Vintage was not a capitalized company, and thus not subject to direct GOB control. He was nonetheless concerned about the requirement to sign a new "service" contract and to give up ownership rights to its production and control over commercialization decisions.

Brazilian, Spanish, and Argentine Actions

¶8. (SBU) The Brazilian Ambassador told Ambassador Greenlee on May 2 that Brazil was not surprised by the terms of the GOB's decree, including its plan to nationalize the Petrobras-owned refineries, but by its timing, as it had interrupted ongoing talks with Brazil and burst the illusion of progress during those talks. He said that the GOB had previously stated that it intended to pay for the refineries, possibly through future concessions to Petrobras, but that it was currently unclear whether or not compensation would be provided, and if so, how much or how. If Petrobras received adequate compensation, he said, it would prefer that the Bolivian government take over 100 percent of the refineries instead of 51 percent. He expressed concern about the unilateral nature of Bolivian policy, the unreasonable tax increase applied to Petrobras, and the decree's provision that gas prices would be established by YPFB, which implied that mutual consent -- as required by the GSA contract between YPFB and Brazil -- would play no role. He was also worried about the requirement to sign service contracts, which Petrobras had already declared it would not do, but acknowledged that Petrobras' real bottom line was not clear. The Brazilian Ambassador gave the Ambassador a copy of an official statement issued on May 2 after the emergency meeting between President Lula, several ministers, and the President of Petrobras (ref A). The statement recognized Bolivia's sovereignty and right to manage its own resources and emphasized maintaining a steady gas supply to (dependent) Brazil, but also noted that private investor rights should be respected. The Brazilian Ambassador told us that these issues would be discussed further in a May 4 meeting between Brazilian President Lula, Argentine President Kirchner, Venezuelan President Chavez, and President Morales.

¶9. (SBU) According to press reports, Petrobras ratcheted up its response on May 3, threatening to halt all investment and bring the GOB to court. Petrobras executive, Arturo Castanos told us on May 4 that the company has not yet filed a trigger letter to begin the arbitration process, but is considering doing so.

¶10. (SBU) According to news reports, Spain has expressed discontent with the decree and plans to send a delegation to Bolivia to discuss the issue. Hydrocarbons Chamber President Menacho told us that Spain is providing considerable support

to Repsol in its negotiations with the GOB. Repsol executive, Miguel Cirbien, told us the company was worried about the 32 percent tax increase imposed on large producers as well as the GOB's plan to take over its Bolivian operation. He said Petrobras was the only company producing more than 100 million cubic feet per day in the two fields to which the 32 percent tax applies, thus Petrobras was the only company that would have to pay the additional tax. Other industry representatives believe that the tax would apply not only to Petrobras, but also to Repsol and Total. Cirbien acknowledged that Repsol had recouped its initial investment, but argued that the company continued to make additional investments since that time. Cirbien said Repsol would continue trying to work with the GOB to clarify what it "really wants."

¶11. (SBU) Comment: Ultimate company decisions to continue playing the GOB's game, pull out, or seek arbitration will depend on the GOB's flexibility in negotiating tax rates, its ability and willingness to pay for company shares, and its definition of "service" provider. Company executives are hoping that President Lula pressures Morales into softening his tone and demands in today's (May 4) meeting. Petrobras' hardening tone has reassured other companies, which intend to ride on Bolivia's largest gas producer's coattails as much as possible. End comment.
GREENLEE